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RHEBAAA/DEPT OF ENERGY WASHINGTON DC  
RUEHRC/DEPT OF AGRICULTURE WASHDC  
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TAGS: [EAGR](#) [EAID](#) [ECON](#) [ETRD](#) [FCSCEG](#) [EG](#)  
SUBJECT: EGYPTIAN GAS, TEXTILE EXPORTS NARROWING TRADE GAP  
WITH U.S. OVER LONG TERM

REF: A. CAIRO 6347 B. CAIRO 4337 C. CAIRO 4167 D.  
CAIRO 5792 E. CAIRO 5779 F. USDOC 5433 G.  
CAIRO 6871

¶1. (U) SUMMARY: ALTHOUGH U.S. EXPORTS TO EGYPT ARE RISING THIS YEAR, BARRIERS TO TRADE ARE LOWERING, AND NEW SECTORS ARE OPENING TO U.S. PRODUCTS, THE U.S. TRADE SURPLUS WITH EGYPT HAS BEEN SHRINKING SINCE 2000, PRIMARILY BECAUSE OF RISING U.S. IMPORTS OF EGYPTIAN NATURAL GAS AND DECLINING EGYPTIAN IMPORTS OF U.S. WHEAT. THESE TRENDS, BOLSTERED BY SOARING EGYPTIAN EXPORTS FROM QUALIFIED INDUSTRIAL ZONE (QIZ) FACTORIES, COULD TIP THE BALANCE OF TRADE TO EGYPT'S FAVOR WITHIN SEVERAL YEARS. HOWEVER, SHIFTS IN THE VOLATILE GLOBAL COMMODITIES MARKETS FOR WHEAT AND NATURAL GAS COULD REVERSE THESE TRENDS IN THE SHORT TERM. THE U.S. TRADE SURPLUS WITH EGYPT WILL LIKELY END 2006 HIGHER THAN IN 2005, ALTHOUGH THE LONG-TERM TRENDS REMAIN IN EGYPT'S FAVOR. END SUMMARY.

¶2. (U) ANNUAL U.S. EXPORTS TO EGYPT FELL FIVE PERCENT FROM 2000 TO 2005, FROM \$3.33 BILLION TO \$3.17 BILLION, WHILE EGYPTIAN EXPORTS TO THE UNITED STATES MORE THAN DOUBLED DURING THAT PERIOD, SURPASSING \$2 BILLION LAST YEAR. AS A RESULT, THE U.S. TRADE SURPLUS FELL FROM \$2.4 BILLION IN 2000 TO \$1.1 BILLION IN 2005, MIRRORING THE TREND IN THE GLOBAL U.S. BALANCE OF TRADE. TRADE IN BOTH DIRECTIONS IS GROWING ROBUSTLY THIS YEAR. THROUGH SEPTEMBER 2006, U.S. EXPORTS TO EGYPT ROSE 31 PERCENT COMPARED TO THE SAME PERIOD LAST YEAR TO \$2.9 BILLION, WHILE EGYPTIAN EXPORTS TO THE UNITED STATES ROSE 40 PERCENT TO \$1.8 BILLION.

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INCREASING SALES OF LIQUEFIED NATURAL GAS (LNG)  
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¶3. (U) INCREASING EGYPTIAN LNG PRODUCTION, COMBINED WITH RISING PRICES FOR OIL AND GAS, HAS DRIVEN THE SHARP INCREASE IN OVERALL EGYPTIAN EXPORTS TO THE UNITED STATES. IN 2000, BEFORE EGYPT'S LNG PRODUCTION CAME ON LINE, MINERAL FUELS MADE UP ONLY 13 PERCENT OF EGYPTIAN EXPORTS TO THE UNITED STATES WHILE IN 2005 THEY CONSTITUTED 51 PERCENT OF EGYPTIAN EXPORTS; NATURAL GAS ALONE ACCOUNTED FOR 36 PERCENT OF EGYPTIAN EXPORTS, AND OIL ANOTHER 15 PERCENT. OVERALL MINERAL EXPORTS INCREASED NEARLY TENFOLD DURING THAT FIVE-YEAR PERIOD.

14. (U) IN THE ABSENCE OF NEW LNG PRODUCTION/EXPORTS FACILITIES COMING ON LINE IN 2007, WE EXPECT A LEVELING-OFF OF THE EFFECT OF LNG EXPORTS ON EGYPT'S OVERALL EXPORTS IN THE COMING YEAR. NEW PROJECTS ARE IN THE WORKS, HOWEVER, INCLUDING A THIRD LNG TRAIN FACILITY ON EGYPT'S MEDITERRANEAN COAST PROJECTED TO OPEN IN 2009. GROWING DOMESTIC DEMAND FOR ELECTRIC POWER -- DEMAND INCREASED 10 PERCENT LAST YEAR -- IS FUELING AN INTERNAL POLITICAL DEBATE OVER WHETHER EGYPT'S GAS SUPPLIES SHOULD BE USED FOR EXPORT VERSUS SUPPLYING THE COUNTRY'S GAS-FIRED, AND SUBSIDIZED, POWER GENERATION SECTOR.

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QIZ PRODUCTION SOARING  
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15. (U) INCREASING EGYPTIAN TEXTILE EXPORTS ARE ALSO ADDING MOMENTUM TO THE SHIFT IN THE BALANCE-OF-TRADE. IN THE FOUR QUARTERS ENDING IN JUNE 2006, AS QIZ FACTORIES BEGAN TO GEAR UP PRODUCTION, THEIR EXPORTS WERE VALUED AT \$508 MILLION, OR 25 PERCENT OF EGYPTIAN EXPORTS TO THE UNITED STATES DURING THAT PERIOD. QIZ FACTORIES CONTINUE TO EXPAND AS THEY SCRAMBLE TO MEET INCREASING ORDERS (REF A), AND TEXTILE EXPORTS WILL ASSUME A LARGER SHARE OF EGYPTIAN EXPORTS TO THE UNITED STATES IN COMING YEARS. AS A RESULT, OVERALL EGYPTIAN EXPORTS WILL BE MORE RESISTANT TO PRICE SHOCKS IN THE NATURAL GAS MARKET, AND THE TRADE TREND IN EGYPT'S FAVOR WILL SOLIDIFY.

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U.S. AGRICULTURAL EXPORTS DECLINING  
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16. (U) WHEAT FARMERS HAVE BEEN LOSING SALES IN EGYPT TO RUSSIA AND UKRAINE IN RECENT YEARS BECAUSE OF THE RELATIVELY HIGH QUALITY, AND HIGH PRICE, OF U.S. GRAIN. OF THE 7 MILLION TONS OF WHEAT THAT EGYPT IS EXPECTED TO IMPORT THIS YEAR, THE GOE'S GENERAL AUTHORITY FOR SUPPLY COMMODITIES (GASC) WILL BUY AROUND 4 MILLION TONS. GASC WHEAT IS USED EXCLUSIVELY FOR THE HIGHLY SUBSIDIZED "BALADI," OR LOCAL, BREAD, A STAPLE ON TABLES ACROSS EGYPT. BECAUSE THE RETAIL PRICE OF BALADI BREAD IS FIXED, AND THE GOE LOSES MONEY ON EVERY PIECE OF PITA IT SELLS, GASC BUYS THE CHEAPEST GRAIN IT CAN FIND, REGARDLESS OF QUALITY.

17. (U) AS A RESULT, FROM 2001 TO 2005 U.S. BULK WHEAT EXPORTS TO EGYPT FELL BY 49 PERCENT TO \$190 MILLION. THAT DROP ACCOUNTS FOR ESSENTIALLY ALL OF THE DROP IN U.S. AGRICULTURAL EXPORTS, WHICH FELL FROM \$1 BILLION IN 2001 TO \$818 MILLION IN 2005. SHIFTS IN THE GLOBAL WHEAT MARKET COULD REVERSE THESE TRENDS IN THE SHORT-TERM: A POOR HARVEST IN THE BLACK SEA WOULD REDUCE GLOBAL SUPPLY AND DRIVE UP PRICES, MAKING U.S. GRAIN MORE COMPETITIVE; OR A BUMPER CROP IN THE UNITED STATES WOULD BRING THE PRICE OF U.S. WHEAT DOWN TO A LEVEL MORE ATTRACTIVE TO GASC BUYERS. BUT THE HIGH U.S. WHEAT PRICES AND RESULTING LOST SALES IN EGYPT REMAIN SYMPTOMATIC OF AN OVERALL U.S. PRICE STRUCTURE THAT IS FUELING THE NATIONAL TRADE DEFICIT.

18. (U) OTHER AGRICULTURAL TRENDS ARE WORKING IN FAVOR OF U.S. EXPORTS TO EGYPT, HOWEVER. THE UNITED STATES REMAINS EGYPT'S TOP SUPPLIER OF CORN, WHILE SALES OF MILK POWDER AND BEEF OFFALS (INTERNAL ORGANS) ARE INCREASING. CONTINUED ECONOMIC GROWTH IN EGYPT COULD ALSO INCREASE DEMAND FOR HIGH VALUE-ADDED AMERICAN AGRICULTURAL PRODUCTS.

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U.S. ASSISTANCE CHANGING  
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19. (U) CHANGES IN ECONOMIC CONDITIONS AND THEIR RESULTING IMPACT ON USAID PROGRAMS ARE ALSO TIPPING THE BALANCE OF TRADE TOWARD EGYPT. IN PARTICULAR, THE COMMODITY IMPORT PROGRAM, WHICH PROVIDED EGYPTIAN COMPANIES ACCESS TO HARD CURRENCY TO IMPORT U.S. MACHINERY AND RAW MATERIALS, HAS BEEN LESS IN DEMAND AS FINANCIAL REFORMS GIVE EGYPTIAN IMPORTERS EASIER ACCESS TO PRIVATE-SECTOR FINANCING (REF B). THE PROGRAM PROVIDED \$270 MILLION IN LOANS TO EGYPTIAN COMPANIES TO PURCHASE U.S. GOODS IN 2002, BUT ONLY \$90 MILLION DURING

THE LAST 12 MONTHS.

¶10. (U) WHILE SOME BORROWERS CONTINUED TO IMPORT U.S. GOODS USING PRIVATE-SECTOR FINANCING, OTHERS SHOPPED ELSEWHERE. U.S. MACHINERY AND TRANSPORT EXPORTS TO EGYPT FELL FROM \$1.4 BILLION IN 2000 TO \$1.1 BILLION IN 2005. FURTHER REDUCTIONS IN THE U.S. ASSISTANCE PROGRAM, WHICH HAS BEEN REDUCED \$40 MILLION A YEAR SINCE 1998, WILL HAVE A CONTINUING NEGATIVE IMPACT ON U.S. EXPORTS TO EGYPT.

¶11. (U) EVOLUTION IN THE \$1.3-BILLION ANNUAL SECURITY ASSISTANCE PROGRAM COULD ALSO REDUCE U.S. EXPORTS TO EGYPT. CURRENTLY 73 PERCENT OF MILITARY ASSISTANCE GOES TO UPGRADES AND MAINTENANCE OF EXISTING U.S. SYSTEMS, DIRECTLY BENEFITING U.S. COMPANIES SELLING MILITARY EQUIPMENT (REF C). IN ADDITION TO THE \$1.3 BILLION ANNUAL MILITARY ASSISTANCE ALLOCATION, EGYPT RECEIVED AN ADDITIONAL \$1.7 BILLION FROM FISCAL YEARS 2001-2005 IN ASSISTANCE PREVIOUSLY ALLOCATED BUT NOT DISPERSED, BOOSTING U.S. EXPORTS DURING THAT PERIOD. NO SUCH ALLOCATIONS ARE EXPECTED IN COMING YEARS.

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EGYPTIANS SHOPPING AROUND  
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¶12. (U) WHEN US AND EGYPT DID NOT LAUNCH FREE TRADE NEGOTIATIONS IN THE SPRING AS THE GOE HAD ANTICIPATED, TRADE MINISTER RACHID RACHID MADE A NUMBER OF PUBLIC COMMENTS ABOUT EGYPT'S INTEREST IN DEVELOPING BUSINESS TIES WITH CHINA, RUSSIA, AND OTHER TRADING PARTNERS. FOLLOWING RACHID'S VISITS TO CHINA AND RUSSIA THIS FALL (REF D), HIS STATEMENTS THAT HE EXPECTED CHINA TO BECOME EGYPT'S LARGEST BILATERAL TRADING PARTNER (VICE THE UNITED STATES) AND THAT HE EXPECTED TO DRAMATICALLY EXPAND EGYPTIAN-RUSSIAN TRADE RECEIVED WIDESPREAD ATTENTION. EGYPT HAS A SIGNIFICANT TRADE DEFICIT

WITH BOTH COUNTRIES, HOWEVER. WHILE EGYPT MAY BE ABLE TO INCREASE NATURAL GAS EXPORTS TO CHINA, IT HAS LITTLE TO OFFER RUSSIA, AND APPEARS TO HOPE PRIMARILY FOR AN INCREASE IN DIRECT FOREIGN INVESTMENT.

¶13. (U) RACHID ALSO SAID THIS SUMMER THAT IN VIEW OF THE SUSPENSION OF THE WTO DOHA ROUND OF NEGOTIATIONS, EGYPT WILL FOCUS ON ITS ARAB AND EUROPEAN PARTNERS WITHIN THE FRAMEWORK OF THE ARAB FREE TRADE AREA AND THE EURO-MEDITERRANEAN PARTNERSHIP (REF E).

¶14. (SBU) THESE STATEMENTS HAVE CONTRIBUTED TO A SENSE OF LACK OF MOMENTUM AMONG U.S. BUSINESSES IN EGYPT. THE U.S. CHAIR OF THE U.S.-EGYPT BUSINESS COUNCIL TOLD USDOC OFFICIALS RECENTLY THAT BILATERAL ACTIVITY IS AT A TEN-YEAR LOW (REF F). CAIRO AMERICAN CHAMBER OF COMMERCE OFFICIALS HAVE ALSO BEEN DISPIRITED BY THE LACK OF PROGRESS TOWARD AN FTA. AND DURING A RECENT TRIP TO THE UNITED STATES WITH OTHER NEA CHIEFS-OF-MISSION TO PROMOTE U.S. TRADE WITH THE MIDDLE EAST, THE AMBASSADOR FOUND WIDESPREAD INTEREST IN THE REGION AMONG U.S. BUSINESSES, BUT A PAUCITY OF INFORMATION ABOUT ECONOMIC CONDITIONS HERE.

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U.S. EXPORTS INCREASING IN 2006  
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¶15. (U) EVEN SO, 2006 HAS BEEN A GOOD YEAR FOR U.S. EXPORTERS TO EGYPT. THROUGH SEPTEMBER, EXPORTS WERE UP 31 PERCENT OVER THE SAME PERIOD LAST YEAR. DRIVING THAT INCREASE IS A 35-PERCENT INCREASE IN MACHINERY AND TRANSPORT EQUIPMENT AS WELL AS A 19-PERCENT INCREASE IN AGRICULTURAL EXPORTS, ALTHOUGH EGYPTIAN EXPORTS INCREASED EVEN FASTER DURING THE SAME PERIOD.

¶16. (SBU) COMMENT: THE NARROWING U.S. TRADE SURPLUS IN EGYPT IS AN UNINTENDED CONSEQUENCE OF A NUMBER OF AMERICAN SUCCESSES: ECONOMIC REFORM SUPPORTED BY THE USG HAS MADE EGYPTIAN IMPORTERS LESS RELIANT ON USG CREDIT; HIGH-QUALITY AMERICAN WHEAT IS TOO EXPENSIVE FOR EGYPTIAN BUYERS; THE EGYPTIAN NATURAL GAS INDUSTRY IS DEVELOPING QUICKLY WITH THE

PARTICIPATION OF AMERICAN AND MULTINATIONAL COMPANIES; AND EGYPTIAN EXPORTERS ARE TAKING EAGER ADVANTAGE OF THE QIZ AGREEMENT TO SELL TEXTILES TO THE UNITED STATES. THEIR SUCCESS IN QIZ EXPORTS MAY PARTLY EXPLAIN A RECENT LACK OF ENTHUSIASM FOR REVIVING THE FTA (REF G). REGARDLESS, THE SURGE IN BIDIRECTIONAL TRADE THIS YEAR INDICATES THAT EGYPT REMAINS A LUCRATIVE MARKET FOR AMERICAN PRODUCTS AND THAT TRADE CONTINUES TO CONSTITUTE A GROWING PART OF OUR BILATERAL RELATIONSHIP. THE CHALLENGE OF U.S. EXPORTERS WILL BE TO RIDE EGYPT'S ECONOMIC EXPANSION WITH SALES OF CAPITAL GOODS. NEW STATE INVESTMENT IN ENERGY AND TRANSPORTATION OFFERS ATTRACTIVE OPPORTUNITIES.

RICCIARDONE